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SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1936

No. 151

MRS. JOHN S. MEADOWS,

Petitioner,

v.

THE IRVING TRUST COMPANY, AS TRUSTEE OF UNITED CIGAR STORES COMPANY OF AMERICA, DEBTOR, ET ALS.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

PERLIE P. FALLON,
Counsel for Petitioner.

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT.

Mrs. John S. Meadows prays that a writ of certiorari issue to review the judgment of the United States Circuit Court of Appeals for the Second Circuit entered on May 21, 1936, affirming an order of the District Court for the Southern District of New York.

OPINIONS BELOW.

The Special Master's certificate is found at R. 242, fol. 724.

There was no opinion in the District Court.

The opinions in the Circuit Court of Appeals are reported in 83 F. (2d) 207.

The opinions in cases of similar issues, heard and decided at the same time, are reported as follows:

In re United Cigar Stores Co. of America (Joseph E. Otis Estate Land Trust et al., appellants), 83 F. (2d) 202.

In re United Cigar Stores Co. of America (City Bank Farmers Trust Co., appellant), 83 F. (2d) 209.

JURISDICTION.

The petition for rehearing was denied on May 21, 1936. The jurisdiction of this Court is invoked under Section 240-(a) of the Judicial Code, and Sec. 25-(c) of the Bankruptcy Act.

QUESTIONS PRESENTED.

(1) Under Sec. 77B (b)-(10) of the Bankruptcy Act, referring to a bankruptcy proceeding pending prior, does the phrase "the surrender of the premises to the landlord", refer to an accepted surrender terminating the lease and allow a claim to a lessor for the damages flowing from such a surrender in a bankruptcy proceeding pending prior?

(2) Where a surrender is accepted after an adjudication in bankruptcy, reserving to the lessor any claims against the bankrupt estate which the Bankruptcy Court may adjudge to the lessor, and thereafter and while the bankruptcy proceedings are pending, the lessee petitions under 77B and its petition is allowed and it recaptures the bankrupt estate, does Sec. 77B (b)-(10) enable the lessor to relate a claim for damages back to the lease in view of the changed status of the decree in bankruptcy and the bankrupt estate?

(3) Under the word "rejection" in the Bankruptcy Act with respect to leases, where a trustee seeks to turn

the lease back to the lessor and it is assigned to a third party by the lessee and a separate agreement is made by the trustee, the lessor and the assignee, which recites a disaffirmance of the lease by the trustee, is there a rejection of the lease sufficient to admit the lessor to any remedy created by Sec. 77B?

(4) Under Sec. 77B (b)-(10) is there an allowable claim on an independent covenant to construct a building upon leased premises at a future date where the lessee is adjudicated a bankrupt and the lease is surrendered with a reservation to the lessor of any claims against the bankrupt estate which the Bankruptcy Court may adjudge to the lessor, and a claim is filed by the lessor in the bankruptcy proceedings and while it is pending undetermined the lessor files a petition under Sec. 77B which is granted?

STATUTES INVOLVED.

The statutes are in an appendix at pp. 14 to 16.

STATEMENT.

The United Cigar Stores Company of America is a corporation of New Jersey. It made a lease of real property at Lincoln, Nebraska, in 1922 (R. 9) and entered into possession. The lease was for 99 years. It contained a covenant that the United would construct a four-story building prior to July 1, 1942 ("Sixth", R. 14). The covenant was personal and the obligation could not be assigned by United without giving security ("Twenty-fifth", R. 30, fol. 90). In August of 1932 United, by a voluntary petition, was adjudicated bankrupt and surrendered its assets to a trustee (R. 88, fol. 263). United was in default at that time as to repairs and taxes. Rent was not paid nor the lease performed

by United after August 29, 1932. The trustee asked that the petitioner, who was the owner of the lease, take the lease back by assignment and give a general release (R. 123, 145, 164). This was not done (R. 160). The trustee obtained an order authorizing it to reject the lease or, in lieu of rejection, to assign the interest of the trustee in the lease to the petitioner or her nominee which the order said was not to constitute an adoption of the lease (R. 162, fol. 486). The petitioner had meantime found a tenant: the Frelem Realty Corporation, a Delaware corporation. Three agreements were then executed. They bear different dates but were delivered together in January of 1933 (R. 71, fol. 211, and R. 73, fol. 218).

(1) The trustee agreed with the petitioner and Frelem Realty Corporation on the charge for use and occupancy with a covenant that the lease had been disaffirmed (Ex. "Q", R. 191).

(2) The petitioner agreed with Frelem Realty Corporation on modifications of the lease reducing the term, the rent, and eliminating the covenant to build. This agreement was made contingent on the following assignment by United (Ex. "R", R. 193, fols. 579, 582, 583, and "I", R. 187, fol. 560):

(3) The petitioner, trustee and United made an agreement by which the United assigned the lease to Frelem, and the petitioner assumed the covenants of the lease. There was a release clause in this agreement—a printed form—which referred to "all claims on the part of the Landlord in respect of rent" (R. 90, fol. 270), "all liability of any nature with respect to the Lease" (R. 91, fol. 271) and "all losses, claims or demands of any nature * * * which may hereafter

arise out of or in connection with the Lease" (R. 91, fol. 271). The petitioner made a reservation by annexing a typewritten Rider as follows:

RIDER.

> "Nothing in this Article Fourth shall be deemed a waiver by the Landlord of the right to prove against the bankrupt estate any provable claims to which the Bankruptcy Court may adjudge the Landlord is entitled but this shall not be deemed to render any claim a provable claim which is not otherwise such or relieve the Landlord from the necessity of proving and obtaining the allowance of any such claim or preclude the Trustee from contesting such proof or allowance. * * *."

The petitioner filed a claim in the bankruptcy proceedings for repairs, taxes and breach of the covenant to build (R. 203, fol. 607). The trustee filed objections which were heard and remained undetermined before the Referee in Bankruptcy (R. 76, fol. 228). The United was not discharged in bankruptcy (R. 80, fol. 239).

In June of 1934 the United filed a petition under 77B which was allowed and the assets then in possession of a trustee in bankruptcy were restored to the United (R. 79, fol. 237). The petitioner filed a claim in the reorganization proceedings under Sec. 77B for the repairs, taxes, breach of the covenant to build and for actual damages not exceeding the rent for three years flowing from rejection of the lease by the trustee in bankruptcy in the prior proceeding (R. 3). The claim was allowed as to taxes and repairs but was disallowed as to breach of the covenant to build and damages flowing from the rejection. The special master held it had been released (R. 242). This was affirmed by the District Court (R. 261). Two judges of the Cir-

cuit Court of Appeals held the claim had been reserved and was within the statute but had been cut off by a surrender of the lease. The third judge held the claim was reserved and also survived any surrender but was not allowable under the terms of the lease.[1]

The judgment is based upon the theory that a cause of action, as defined by State law, must exist at petition filed; that the bankruptcy pending prior and the United's status as a bankrupt, and its acceptance of a new status are to be disregarded; that the rights cannot be reserved under the bankruptcy power alone.

SPECIFICATION OF ERRORS.

The Circuit Court of Appeals erred in holding that:

1. Sec. 77B (b)-(10) did not use the term "surrender of the premises" in the sense of an accepted surrender or act of the trustee in the process of rejection.

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[1] The lease contained the covenant to build, a covenant for the deposit of $25,000 if United assigned before building, and a covenant for the deposit of insurance moneys in case of fire. A clause was inserted that if United defaulted these would revert to lessor ("Twentieth", R. 28, fol. 82). None of these covenants had come into operation at the time of the default. There was a further clause protecting the lessor in the event no security came into being. It is the last sentence of "Twenty-seventh" as follows:

> "Lessee covenants that the rights and remedies of lessor under this lease shall be cumulative and no one of them shall be exclusively of any of the rights or remedies provided for in this lease or otherwise allowed by law" (R. 33, fol. 99, at p. 34, fol. 101).

The Nebraska law treats a tenant in default as a holdover and allows the lessor to relet in the absence of express provision in the lease.

The concurring opinion reads the lease as if the latter clause and the local law were non-existent.

2. Sec. 77B does not contemplate a bankruptcy pending prior and the return of the assets in determining allowable claims for damage to a lessor by bankruptcy in a proceeding pending prior.

3. The Bankruptcy Act does not contemplate a rejection when the trustee does not adopt a lease as an asset of the estate, repeatedly asserts it must be taken back, obtains an order for that purpose, repeatedly requires the petitioner to certify it was disaffirmed and joins in an agreement by which the lessee assigns it to a third party.

4. An independent covenant in a lease is not a provable claim under Sec. 63 as it read on August 29, 1932, and a claim pending in bankruptcy proceedings did not become allowable under Sec. 77B when that section was made operative.

5. In affirming the order of the District Court.

The petitioner assigned as error in all of the lower courts:

1. That the claim survived any surrender by express provision of 77B ("b", R. 275, fol. 823, in subdivision "4", R. 276; fol. 826).

2. That the proper construction of the statute was that the claim for damages related back to the lease ("1", R. 265, fols. 795, 796, 797, and "4", R. 268, fols. 802 to 807).

3. That the decree in bankruptcy, recited in the agreement relied upon by the objectors, had been modified by proceedings under 77B ("11", R. 274, fol. 821; Exceptions p. 84, fols. 251, 252, 253; also, "d", R. 268, fol. 804).

4. That the United had shifted from one insolvency proceeding to another and recaptured its assets ("e", R. 269, fol. 805; also, "8", R. 273, fol. 819).

5. That the lease had been rejected in law ("2", R. 267, fol. 799).

6. That the covenant to build was a provable and allowable debt under Sec. 63 (a)-(4) ("6", R. 272, fol. 816, and "7", R. 273, fol. 817).

REASONS FOR GRANTING THE WRIT.

(1) The judgment involves the legislative intention with respect to the construction of Sec. 77B (b)-(10) of the Bankruptcy Act, with respect to bankruptcies pending prior and the word "surrender" as used therein, an important question of Federal law which has not been, but should be, settled by this Court. The decision below is based on the premise that Congress intended that where there had been surrender in a proceeding pending prior, there is no allowable claim. It, also, interpreted "surrender" to refer to an act of the parties rather than an act of the trustee in the process of rejection. Sec. 77B (b)-(10) provides that a person injured by the rejection of a lease by a trustee in bankruptcy *"in a proceeding pending prior"* shall be a creditor, and defining the claim states that "the claim shall be limited to an amount not to exceed the rent, without acceleration, for the three years next succeeding the date of the surrender of the premises to the landlord" which are immediately followed by the words "or the date of reentry of the landlord" which is an act terminating a lease as a matter of law and which are immediately followed by the words "whichever first occurs whether before or after the filing of the petition" and which are then immediately followed by the words

"plus unpaid rent accrued up to such date of surrender or reentry", the last phrase stating the rule of law as to a lessee's rent liability where a lease is terminated by an accepted surrender or reentry. *American Bonding Co.* v. *Pueblo Inv. Co.*, C. C. A. 8, 150 Fed. 17, 30. The language is directed to a claim for damage, as distinct from rent. The limitation stops rent, as such, with reentry or recovery of possession. It makes no distinction between processes of repossession. It creates an equitable damage claim arising in the change from bankruptcy to reorganization which survives surrender or reentry in a proceeding pending prior by legislative direction and United's voluntary acceptance of the statute. A claim for damage survives surrender where parties accept that condition. *Hall* v. *Gould*, 13 N. Y. 127, 134; *Daynes-Beebe Music Co.* v. *Chase*, C. C. A. 8, 23 F. (2d) 648, 651; *Kottler* v. *New York Bargain House*, 242 N. Y. 28, 33.

(2) There are grounds for this Court's supervision. The assets were placed beyond the reach of creditors by one decree, they were restored by a later decree, and a third decree—the judgment here—ousted the petitioner of all remedy. This was done under the bankruptcy power and in disregard of petitioner's reservation in the Rider of any rights the bankruptcy power might give. The United was obligated upon over 1,000 leases (R. 248, fol. 742). The special master found that "the bankruptcy herein was based upon the lease situation" (R. 257, fol. 771). By a voluntary petition the United was adjudicated. After the United and its trustee had made arrangements with respect to leased properties, the United reassumed possession of its assets by a petition under Sec. 77B. The arrangement with petitioner was made by a writing reciting the decree of the

United States court that the United was insolvent and had surrendered its assets ("3", R. 88, fol. 263). The petitioner acted upon the full faith and credit of the decree. Historically, no debtor had been permitted to avoid its obligations and recapture its assets by shifting from one imperfect insolvency proceeding to another. *In re Stephenson,* 20 Q. B. 540, 544; *The Citizens Fire, Marine & Life Ins. Co.* v. *Wallis,* 23 Md. 173, 184; *Turner* v. *Brown,* 3 Common Bench 157, 136 Reprint 63; Bankruptcy Act, Sec. 12-(e). Congress avoided such a result here. It recognized the change of status by express reference in Sec. 77B (b)-(10) to a bankruptcy pending prior. When adopted by petition it was retroactive, 77B-(p).

The construction of the lower court requires lessors under Sec. 77B and Sec. 63, as amended, to avoid surrender, the rules of which vary in different States and thereby create differences of right under a statute intended to be uniform. Properties will be left idle and rent will run to avoid a forfeiture. The legislative intention was that rent, as such, was to stop and the properties be returned to economic productivity and damages be reduced—a construction which is in the public interest. *Charles Warren, Bankruptcy in United States History.* The judgment is the exact opposite of the legislative direction.

The rights of many citizens in many States are involved in the present litigation. The result has been obtained under decrees of United States courts in bankruptcy and a United States statute. The relation of the statute to the prior proceedings should be declared by this Court.

(3) The judgment holds that a surrender may be implied in law where there is an express surrender in

writing between the parties and is inconsistent with the decisions of this Court in *Klebe* v. *United States,* 263 U. S. 188, 192, which held a contract will not be implied where the parties act by an express contract, and *Beall* v. *White,* 94 U. S. 382, 389, which held an express surrender repells implied surrender, and the weight of authority, *Kottler* v. *New York Bargain House,* 242 N. Y. 28, 35.

The judgment, in refusing to consider the reservation of the Rider in connection with all of the clauses in the agreement and the entire transaction, is inconsistent with the decision of this Court in *Miller* v. *Robertson,* 266 U. S. 243, 251, which held an agreement must be construed as a whole and in the light of all of the circumstances. It is inconsistent with the local public policy, *Compiled Statutes of Nebraska,* ch. 76, Art. 1, Sec. 109, which declares that agreements relating to real property be construed as a whole, and many authorities in the Federal courts, *Woolworth Co.* v. *Petersen,* 78 F. (2d) 47, 48, C. C. A. 10. Agreements which refer to each other are construed together. *Male* v. *Lafferty,* 105 Fed. Rep. 564, 565. The acceptance of the surrender was conditional. The petitioner reserved by the Rider any rights which the bankruptcy power might create in her for the damages she had sustained. It rested in the bankruptcy power to create a new remedy since the bankruptcy was vacated and the assets restored to United. The United adopted the remedy created by filing a voluntary petition under the section, *Knoxville Water Company* v. *Knoxville,* 189 U. S. 434, 437; *Calhoun* v. *Massie,* 253 U. S. 170, 177, which held that where a statute is adopted to obtain its benefits, the burdens go along.

The judgment, in holding that the trustee did not reject the lease, was inconsistent with the decision of

this Court in *Dushane* v. *Beall,* 161 U. S. 513, 516, which held that lack of action by a trustee in assuming the lease as an asset, was a rejection. The trustee did not adopt the lease, required the petitioner to certify it was disaffirmed (Ex. "Q", R. 191, fol. 571); and to reaffirm the rejection in an amendatory agreement (paragraph "Second", Ex. "2", R. 98, fol. 293, which reaffirms the last sentence of paragraph "Fifth" of Ex. "1", R. 91, fol. 273) and indicated that the lease was not claimed as an asset of the estate. *Smith* v. *Gordon,* 22 Fed. Cas. 554, headnote "8".

The claim on the covenant to build was an independent, personal covenant of the United. It was separate from the agreement to pay rent ("First", R. 9, fol. 26). The United could only release itself by depositing security ("Twenty-fifth", R. 30, fols. 90, 91, 93). It was an allowable claim under Sec. 63. It was reserved by the Rider. The judgment below that it was not allowable under Sec. 63 is inconsistent with the decision of this Court in *Irving Trust Co.* v. *A. W. Perry,* 293 U. S. 307, 311, which held an independent covenant in a lease was an allowable claim under Sec. 63, and the decision of the Circuit Court of Appeals for the Seventh Circuit in *Towle* v. *Pullen,* 238 Fed. Rep. 107, 110, which held such a building covenant was a separate independent covenant, and the decision of the Circuit Court of Appeals for the Fifth Circuit in *Trust Co. of Georgia* v. *Whitehall Holding Co.,* 53 F. (2d) 635, 636, which held a separable covenant was allowable under Sec. 63. That certiorari was denied in *Tipton et al.* v. *Irving Trust Company,* 74 F. (2d) 45, 295 U. S. 747, does not answer the point because there the covenant was inherent in the lease and not independent. The holding that it was not a valuable claim is inconsistent with the

local law declared in *Gustin* v. *Nebraska Building & In. Co.,* 110 Nebraska 241, which allowed recovery of damages for breach of such a covenant, and the decisions of the Sixth Circuit Court of Appeals in *O'Brien* v. *Illinois Surety Co.,* 203 Fed. 436, 440 and 223 Fed. Rep. 933, which allowed damages for breach of a similar covenant.

WHEREFORE, it is respectfully submitted that this petition should be granted.

Dated June —, 1936.

PERLIE P. FALLON,
Counsel.

APPENDIX.

(1) Bankruptcy Act, July 1, 1898, C. 541, 30 Stat. 563, as amended July 7, 1934, C. 424, 48 Stat. 912; as amended Aug. 20, 1935, C. 577, 49 Stat. 664; Aug. 29, 1935, C. 809, 49 Stat. 965:

"SEC. 77A. *Additional Jurisdiction.*—In addition to the jurisdiction exercised in voluntary and involuntary proceedings to adjudge persons bankrupt, courts of bankruptcy shall exercise original jurisdiction in proceedings for the relief of debtors, as provided in section 77B of this Act." (U. S. C. App., Title 11, Sec. 206.)

"SEC. 77B * * * (b) * * * (10) * * * The term 'creditors' shall include for all purposes of this section and of the reorganization plan, its acceptance and confirmation, all holders of claims of whatever character against the debtor or its property, including claims under executory contracts, whether or not such claims would otherwise constitute provable claims under this Act. The term 'claims' includes debts, securities, other than stock, liens, or other interests of whatever character. * * * In case an executory contract or unexpired lease of real estate shall be rejected pursuant to direction of the judge given in a proceeding instituted under this section, or shall have been rejected by a trustee or receiver in bankruptcy or receiver in equity, in a proceeding pending prior to the institution of a proceeding under this section any person injured by such rejection shall, for all purposes of this section and of the reorganization plan, its acceptance and confirmation, be deemed to be a creditor. The claim of a landlord for injury resulting from the rejection of an unexpired lease of real estate or for damages or indemnity under a covenant contained in such lease shall be treated as a claim ranking on a parity with debts which would be provable under section 63 (a) of

this Act, but shall be limited to an amount not to exceed the rent, without acceleration, reserved by said lease for the three years next succeeding the date of surrender of the premises to the landlord or the date of reentry of the landlord, whichever first occurs, whether before or after the filing of the petition, plus unpaid rent accrued up to such date of surrender or reentry: * * *." (U. S. C. App., Title 11, Sec. 207.)

"SEC. 77B * * * (o) In proceedings under this section and consistent with the provisions thereof, the jurisdiction and powers of the court, the duties of the debtor and the rights and liabilities of creditors, and of all persons with respect to the debtor and its property, shall be the same as if a voluntary petition for adjudication had been filed and a decree of adjudication had been entered on the day when the debtor's petition or answer was approved." (U. S. C. App., Title 11, Sec. 207.)

"SEC. 77B * * * (p) This section shall take effect and be in force from and after the date of the approval of this amendatory Act and shall apply as fully to debtors, their stockholders and creditors, whose interests or debts have been acquired or incurred prior to such date, as to debtors, their stockholders and creditors, whose interests or debts are acquired or incurred after such date. Proceedings under this section may be taken in proceedings in bankruptcy which are pending on the effective date of this amendatory Act." (U. S. C. App., Title 11, Sec. 207.)

(2) Bankruptcy Act, July 1, 1898, C. 541, 30 Stat. 562:

"SEC. 12 (e) Upon the confirmation of a composition, the consideration shall be distributed as the judge shall direct, and the case dismissed. Whenever a composition is not confirmed, the

estate shall be administered in bankruptcy as herein provided." (U. S. C., Title 11, Sec. 30).

"SEC. 63. *Debts which may be proved.*—(a) Debts of the bankrupt may be proved and allowed against his estate which are (1) a fixed liability, as evidenced by a judgment or an instrument in writing, absolutely owing at the time of the filing of the petition against him, whether then payable or not, with any interest thereon which would have been recoverable at that date or with a rebate of interest upon such as were not then payable and did not bear interest; * * * (4) founded upon an open account, or upon a contract express or implied; * * *.

(b) Unliquidated claims against the bankrupt may, pursuant to application to the court, be liquidated in such manner as it shall direct, and may thereafter be proved and allowed against his estate." (U. S. C., Title 11, Sec. 103).

(3) Compiled Statutes of Nebraska, 1929, Ch. 76, Art. 1, Sec. 109:

"76-109. *Construction of Instruments, Duty of Courts.*—In the construction of every instrument creating or conveying, or authorizing or requiring the creation or conveyance of any real estate, or interest therein, it shall be the duty of the courts of justice to carry into effect the true interest (intent) of the parties, so far as such intent can be collected, from the whole instrument, and so far as such intent is consistent with the rules of law."